EXHIBIT 48

From:	Porco, Laura
Sent:	Friday, May 22, 2009 1:09 PM
To:	Naggar, David; Freed, Ian; Mcintosh, Madeline; Kessel, Steven; Marine, Jay
Subject:	RE: The Shatzkin Files
Follow Up Flag:	Follow up
Flag Status:	Completed
Attachments:	Musings on Pub Economics.docx

The Pub Lunch Cader article related to this that is referenced is below. If you want to send to your kindle all the articles on the topic, I've attached a word file. ...such great holiday reading.

Laura

The eBook Pricing Problem

Over the weekend the NYT ran a week in review piece looking at the surface issues and concerns for both readers and publishers as a result of Amazon's efforts to make $9.99 the standard ceiling for new and popular hardcovers in ebook versions.

Author David Baldacci says "unfortunately there won't be anyone selling it anymore because you just can't make any money." Simon & Schuster ceo Carolyn Reidy asserts that "what a consumer is buying is the content, not necessarily the format." And Harper ceo Brian Murray says "If prices come down but the overall market is bigger, then we should be O.K. But if prices come down and the market doesn't grow, then we can't make money."

In related blog posts, Mike Shatzkin added some "facts and nuance that the article didn't cover." The jist is that the iPhone platform is already disrupting Kindle's deviced-locked model, which will also compete more and more with a complex environment of ebook retailers, devices and platform options, but also that people always talk about how publishers' costs should change for ebooks but never note that "the costs for retailers evaporate as well when they don't have to invest in inventory or handle physical goods."

Separately, Evan Schnittman reminded readers of his argument that the real problem with ebooks going mainstream isn't the list prices but the way that they will shift big chunks of cash flow from upfront (on shipment of books when they first go to market) to after individual sale to consumers. (In essence, it's the same as the shift to scan-based compensation that scares publishers on their physical books already.)

The data we published in February in "Paid Is More Complicated Than You Think" still holds; in fact 30 percent of all Kindle titles sell for more than $9.99 (and 6 percent are virtually free, selling for a penny or nothing). But, as we confirmed in our survey of recent Kindle sales data, top-of-the-list fiction is selling in very strong ratios of Kindle to print editions at Amazon.

We've been looking at the price issue, understanding how deeply it concerns publishers, and as usual have a different take on it. The summary points are:

1. Selling terms likely can and should change, but publishers will need to take the lead

2. Parity ebook prices strengthen Amazon, and inhibit competition--which is directly contrary to publishers' interests.

3. The economics for publishers of lower-priced ebooks are better than people think

4. It's probably the authors who have more to worry about

5. The real problem isn't making enough money on ebooks; it's that inexpensive ebooks hasten the downfall of physical retail

Here are the expanded arguments:

1. Per Shatzkin's quote above, ebooks reduce operational costs for retailers as well as publishers. In setting lower ebook prices, Amazon has effectively admitted that ebook discount schedules should be lower by giving the surplus discount to their customers. Thirty percent is prevailing retailer discount on digital music sales now, and companies like Scribd are introducing the notion that at least some digital print retailers are happy to sell publishers' product at a twenty percent discount.

When and how will the showdown come? Many players seem to understand that a lower ebook discount schedule will be a fact of life at some point. Publishers should consider making that move sooner rather than later, and the extra discount makes it much easier to set lower ebook list prices. Plus, isn't it easier to take a firm stand on discount now, before the market has grown further?

2. In the short term, publishers are doing just fine by pricing ebooks at parity to, or just slightly less than, print books. After all, Amazon is willing to take a loss (or very small margins) on their Kindle units, and what publishers perceive is that their high ebook list prices are not impeding sales growth.

But that's a short-term strategy that only strengthens Amazon's position in this growing market. It's a little like the UK book market, where publishers' bottom line has stayed strong as they give huge discounts to supermarkets and discounters while raising retail prices--except that those higher prices are hurting all of the full-line booksellers that carry a wide range of books and support the whole list.

In the emerging ebook landscape, publishers will benefit from a complex landscape of devices, platforms and retail and wholesale partners--it preserves an important role for them to play.

But parity ebook pricing hurts all of those emerging players and potential competitors to Amazon who are less able or willing to take a loss on ebook sales.

Lower ebook pricing may hurt your short-term results--but while the market remains small, you can afford that if it encourages the competition that will protect you for the future.

3. For many people this is the biggie. Some people reason that the only "cost savings" of ebooks for publishers is the elimination of printing, which they figure reduces the price by about $2. Consumers instinctively know that doesn't make sense, and here are the numbers that prove it. By our reckoning, you could cut your ebook prices by at least 40 percent, at standard discounts, and still make approximately the same money. (And we know of at least one publisher that is about to do this very thing.)

Here's how it works. Figure that eliminating PP&B saves 8 to 10 percent of the retail price--but that's 16 to 20 percent of your gross receipts. Then you also have to count the elimination of returns. On average, getting rid of the excess physical inventory and just the handling of that inventory would save at least another 10 percent of gross. Looked at another way, though, Harper Studio has effectively told accounts its worth 10 points of discount, or 20 percent of gross, to eliminate returns and do all business nonreturnable.

As publishers move to paying authors 25 percent of receipts for ebooks instead of basing royalties on retail prices, on a p&l for a successful hardcover, the publisher would pick up another 5 percent of receipts for the ebook version. And if you are a distributed publisher--as most are--your distributor is going to charge you less for your ebook sales. As well they should, since you have eliminated the physical warehousing and streamlined the trade sales process. Understandably, big publishers operating their own physical warehouses alongside digital warehouses may not see themselves as gaining any "savings" since they still need to keep

the regular warehouse going but most publishers and should allocate savings here. (We could not get a firm figure from distributors on how much lower there are e-distribution charges run.)

Add it up and you are looking at savings of between 35 percent and 50 percent of gross receipts. Which means publishers can basically reduce their ebook prices by the same amounts--lets settle on a target of 40 percent--and still net the exact same dollars. That's without assuming any increase in sales based on lower retail price, and it doesn't touch the money for all other parts of the publishing process.

4. So publishers can actually maintain their gross dollars from lower ebook pricing. Currently, it's the authors who would suffer the most. Lower prices do mean lower royalties--whether you are getting paid on list or on gross.

As agents and authors have been arguing since the beginning of the ebook world, royalties need to rise, or at least change, if we don't want authors to suffer in a world of lower prices.

For publishers and authors to win together, ebook prices need to come down and the discount schedule has to get shorter, providing more margin to adjust the sharing of the proceeds.

(Shatzkin has suggested separately that in an ebook world, authors should think about being compensated with a fixed amount per unit regardless of retail or wholesale price and discounts.)

Rethinking price and discount will lead to reexamining other long-held beliefs as well. Customers have in fact been taught ever since the introduction of the paperback that containers of different quality (hardcover; mass; trade paper) have very different costs and prices, just as they've been taught that time affects price (e.g. new releases usually cost more).

We can see a world in which all of your books are priced according to simple formulas: new releases are all at one price point, and backlist of a certain age is all at another price point. And there's a promotional window in-between that relates to how long the title has been on the market.

5. So we can envision logical scenarios in which publishers and authors can still generate the same dollars--or better if lower prices stimulate more sales--from ebooks.

The knottier problem, as the NYT hinted, is that "the doomsday scenario for publishing is that the e-book versions cannibalize higher-price print sales."

This strikes me as the real problem in a transitional world, particularly as publishers are suspecting that low Kindle prices are taking market share away from print on their big fiction releases in particular. As we know, a small set of big books support the sales volume and overheads for publishers and many physical retailers alike. If you reduce sales (and increase returns) on that relatively small set of print books, you potentially threaten physical retailing in general, which has enough problems as it is. I don't have a smart answer here yet, but it's probably why some publishers are thinking about whether to delay the release of some books in ebook form rather than put them on the market ahead of print publication.
NYT
Shatzkin post
Schnittman post

From: Naggar, David
Sent: Thursday, May 21, 2009 8:46 PM
To: Freed, Ian; Mcintosh, Madeline; Porco, Laura; Kessel, Steven
Subject: FW: The Shatzkin Files

This guy has lots to say and is often quoted by Cader...

From: noreply+feedproxy@google.com [mailto:noreply+feedproxy@google.com] **On Behalf Of** The Shatzkin Files
Sent: Wednesday, May 20, 2009 11:06 PM
To: Naggar, David
Subject: The Shatzkin Files

The Shatzkin Files

Another thought about how deals might change in the ebook value chain

Posted: 20 May 2009 05:17 AM PDT

There has been a lot of discussion about ebook pricing lately. I did **a post following Motoko Rich writing about this in the Times**, but **Rich's post itself** was a sign of the discussion taking place, not the catalyst for it. Today in Publishers Lunch, Michael Cader runs through some calculations to demonstrate that when publishers shed the costs of printing the books they sell as well as the costs of warehousing them, printing books they don't sell, and handling returns on books they thought they'd sold, they can reduce retail prices by 40-50% and still be taking in the same number of margin dollars.

Cader points out that there is a different problem of unintended consequences: if a lot of business shifts to ebooks, then the critical mass requirement for many brick-and-mortar stores might not be met and we'll develop a downward spiral of printed book exposure and sales. That's an accurate point, but I can't see too many people trying to slow down the growth of ebook sales to address it.

We have suggested here that publishers should be reducing the discounts offered to retailers because, as much as publishers' costs go down moving from print to digital, so do retailers'. And because retailers have a (sensible) penchant for turning excess margin into consumer discounts, the discounts being offered lead to a very tenuous situation for publishers. Many retailers are living with just the margin they probably need, but they're doing it *voluntarily*. The low price the consumer is getting is because of retailer policy, not publisher policy. If the publisher sells downloads directly at the same price, the retailer is (justifiably) going to say "hey, the discount you offer me is supposed to be off the *publisher's price*, so if you sell at discount, don't you owe me some money?

The widely-remarked on Amazon Kindle pricing underscores this point. Amazon is buying ebooks (for the most part) at 50% of the publisher's suggested retail. But then they're giving away much of, all of, or even *more* than that margin to give the consumer a lower price (often the billboard price of $9.99.) Nobody expects Amazon to sustain this sell-at-a-loss strategy forever. And few expect Amazon to raise prices to the consumer. That leaves one alternative: use the leverage of all those Kindle owners to get reduced prices from the publisher.

And that's why, in their own interests, publishers have to reduce retail discounts across the board.

Authors are facing a different margin pressure. Publishers generally find it easier to reduce the author's take than the retailer's so, even before putting pressure on retail discounts, they have been reducing author royalties. Just a few years ago, there was bold talk from the author side that a 50-50 split of ebook revenues between publisher and author made sense. But it seems that the "standard" for

ebook royalties has settled in at 25%, or even 15%, of publishers' receipts. Since discounts are about 50%, that amounts to 7.5% to 12.5% of retail, which is hardly a bonanza for the authors. And remember, many informed voices are clamoring for that suggested retail price for ebooks to come *down*!

It is because the market is young and the flux is still great that I suggest that publishers should be rethinking intermediary discounts. For the same reason, it is also time for authors and their agents to be rethinking the royalty rules. Expressing royalty as a percentage of either retail price or net receipts is a concept that makes a certain amount of sense in the physical world, where the cost of manufacturing creates an anchor for pricing. There is a certain minimum price below which publishers won't go when they have to pay to print books. And bigger, fatter books, which cost more to print and would drive up both retail price and royalty, also imply a greater contribution of IP by the author.

But in the virtual world, perhaps it would work better for everybody if authors negotiated to get a flat number of dollars (or cents) per unit sold. Publishers should really have no problem handling this: they've been working with pricing with a known cost-of-goods higher than zero for a very long time. And, for authors, it would eliminate the possibility that diminishing ebook prices will lead to royalties which by historical standards are laughable and for an author trying to make a living are unsustainable.

This practice will probably arise when agents see the need to negotiate a *mimimum* dollars or cents royalty per ebook sold to protect against overly-aggressive promotional pricing, which is already proving to be a temptation for publishers with no physical cost of goods and with author royalties that decline with price. With Scribd offering 80% of the retail price and Smashwords offering 85%, authors will calculate very quickly how low their prices could be to yield the same return (or maybe, twice as much return) for each copy sold than what is the standard offering now. When Scribd and Smashwords files are as easily secured for the iPhone as anybody else's, the agents will have a very hard time convincing their authors to accept things as they are.

Posted this originally without a reminder about Thursday, May 28 at BEA: "Stay Ahead of the Shift." AND there are two panels I'm moderating you'll want to see. On Thursday at 3, Brian O'Leary, Laura Dawson and I are doing "XML for Editors." And on Friday morning at 9:30, I'll moderate "Digital Debuts Tool Time" with the leaders of at least three great new propositions on the stage with me: Hugh McGuire of BookOven, Mark Coker of Smashwords, and Peter Clifton of Filedby.

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